United States Court of Appeals

for the Second Circuit

APPELLANT'S REPLY BRIEF

75—7648

United States Court of Appeals

FOR THE SECOND CIRCUIT

No. 75-7648

B

In the Matter of

WEIS SECURITIES, INC.,
Debtor.

P/S

STOCK CLEARING CORPORATION,
Plaintiff-Appellant,

—against—

WEIS SECURITIES, INC., and EDWARD S. REDINGTON,
as Trustee of Weis Securities, Inc.,
Defendants-Appellees.

APPEAL FROM THE DISTRICT COURT OF THE UNITED STATES
FOR THE SOUTHERN DISTRICT OF NEW YORK

REPLY BRIEF OF APPELLANT

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4

TABLE OF CONTENTS

	PAGE
I. Both the Trustee and SIPC have Mischaracterized the Prior Proceedings: This Case Comes To This Court After a Summary Adjudication, There Was No Trial Below and There Are No Findings of Fact on the Disputed Issues Here	1
II. Both the Trustee and SIPC Urge Affirmance With Factual Arguments Unsupported and Unsupportable On The Summary Judgment Record Made Below	7
Conclusion	10

Table of Cases

American Mfr. Mut. Ins. Co. v. *American Broadcasting-Paramount Theatres, Inc.*, 388 F.2d 272 (2d Cir. 1967)	6
Chanofsky v. *Chase Manhattan Corp.*, Dkt. No. 75-7288 (2d Cir., Mar. 1, 1976)	6
Home Ins. Co. v. *Aetna Casualty & Surety Co.*, Dkt. Nos. 75-7357, 75-7359 (2d Cir., Jan. 13, 1976)	6
Jaroslawicz v. *Seedman*, Dkt. No. 75-7299 (2d Cir., Dec. 19, 1975)	6
Judge v. *City of Buffalo*, 524 F.2d 1321 (2d Cir. 1975)	6
Painton & Co. v. *Bourns, Inc.*, 442 F.2d 216 (2d Cir. 1971)	5-6
In re Perpall, 256 Fed. 758 (2d Cir. 1919)	9, n
United States v. *Bosurgi*, Dkt. Nos. 75-6013, 75-6053 (2d Cir., Jan. 29, 1976)	6

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I

Both the Trustee and SIPC have Mischaracterized the Prior Proceedings: This Case Comes To This Court After a Summary Adjudication, There Was No Trial Below and There Are No Findings of Fact on the Disputed Issues Here.

Both the brief of the Trustee and that of SIPC are founded on the same fundamentally flawed premise: that the disputed facts in this case have been determined by the Courts below. Thus, the Trustee argues (Tr. Br. 14) that "[t]his case was . . . decided after trial on a stipulated

record" and claims "[n]either party made any motion for summary judgment." Similarly, the Trustee terms (Tr. Br. 4) the hearing date set by the Bankruptcy Court for oral argument on the written submissions of the parties as the "date set for trial."

This position is untenable. As the Trustee admits (Tr. Br. 15) at the hearing, "Judge Babitt went on to characterize the posture of the case as 'basically a motion for summary judgment by both sides.' " Reference to the Hearing Transcript (A-157) will show that in pursuit of this understanding Judge Babitt and the Trustee's counsel engaged in the following colloquy:

> "The Court: And, I could grant summary judgment to either side, either dismiss the complaint or grant the relief sought by the complaint under Rule 56, is that correct?
>
> [Trustee's Counsel]: That's correct.
>
> The Court: Then all we have, then, are straight questions of law...."

To be sure there was a stipulation of fact, but it did no more than establish the terms of the contract between SCC and Weis and some of the facts regarding the events of May 24, 1973. It provided the necessary predicate for SCC's summary judgment motion. SCC argued to the Bankruptcy Court that since the agreement between SCC and Weis, on its face, provided for delivery of securities to Weis against payment in cash, SCC was entitled—as a matter of law—to reclaim them when Weis did not fulfill its part of the contract and failed to make payment. SCC also argued that it was likewise clear from the face of the agreement that it had standing to reclaim because it had paid for the securities pursuant to Rule 7 and because it was a bailee of those securities.

The decision called for was one restricted to what could be discerned from the four corners of the contract—in the

absence of complete discovery, without live testimony and without a full hearing on the issue of the contracting parties' intent as expressed in their agreement and as manifested by their conduct on the date in question.

The Bankruptcy Court, however, failed to address the issues as presented and instead—as observed by SIPC (Br. 3, 4-5)—erroneously decided the case "on the merits", holding (A-166, A-167) that SCC had made an insufficient showing to sustain its claim to reclamation. As the Trustee concedes (Tr. Br. 15), the Bankruptcy Court simply did not rule on SCC's motion or restrict its adjudication to the issue of contract interpretation framed by the opposing motions but rather "found that SCC had failed to sustain its burden of proof, and therefore . . . dismissed the complaint"—hardly a proper conclusion on a summary judgment motion.

Doubtless aware of the vulnerability of the Bankruptcy Court's disposition of SCC's motion, the Trustee makes no effort to support or justify that Court's ruling. Rather, the Trustee accuses (Tr. Br. 14) SCC of mischaracterizing the procedural posture of this case and asserts (*Ibid.*) that the decision below was proper because made after a trial. In doing so, the Trustee repudiates his previously acknowledged understanding (see p. 2, *supra*) and takes issue with Judge Babitt's observation that this case is one involving summary judgment, by asserting without the slightest record support: "Of course, what really happened was a trial on a stipulated record . . ."

Seeking to further advance this thesis, the Trustee seizes (Tr. Br. 15) upon some language from SCC's Memorandum on Appeal submitted to the District Court in which SCC explained:

> "Because there is no dispute as to the facts, the *legal issues* presented to the Court below, including the question of standing, are now properly before the Court." (emphasis supplied).

But, that of course is exactly what SCC has argued here (see Appellant's Brief, pp 9-14). On appeal, the District Court was indeed presented with two sharply drawn legal issues: (a) whether SCC's standing to sue could be discerned, as a matter of law, from its role in the transaction; and, (b) whether the contract was so unambiguous in providing for a cash transaction as to entitle SCC to judgment and reclamation of its securities.

The District Court compounded the error of the Bankruptcy Court. Rather than deciding either of the pure propositions of law before it, it attempted to dispose of this case by deciding the disputed issue of whether a cash transaction was intended by seeking, without benefit of a trial record, to discern the underlying intent of the parties as to the application of Rule 7 on May 24, 1973. This was clear error.*

Acting like a trial court, the District Court below determined (A-178 to A-179)—without benefit of a record directed to the issue of the meaning, purpose and intention underlying SCC Rule 7 or SCC's other rules—that the settlement procedures of SCC had some unspecified and unexplained credit characteristics that resembled the day loans that commercial banks commonly extend to the brokerage community.

Like the Bankruptcy Court, the District Court made no findings of fact. Instead, the District Court relied on the following observations, none of which has any specific record support:

---

* Contrary to SIPC's contention (SIPC Br. 2, 7), the District Court did not adopt the Bankruptcy Court's rationale, it founded its decision entirely upon the conclusion, unsupported by the record, that the underlying intent of Rule 7 was to effect settlement on credit rather than as a cash transaction. (A-178-A-179). As for the Bankruptcy Court's reasoning, as both the Trustee and SIPC observe (Tr. Br. 4, SIPC Br. 2, 7), the District Court in its seven page opinion (A-173 to A-180) said only (A-179) that the Bankruptcy Court's "ruling seems sound . . ."

(1) "SCC was not dealing with strangers, with members of the general public. It was dealing with members of NYSE [New York Stock Exchange] whose financial condition was being monitored by that institution." (A-178)

(2) "Clearing members were permitted to take away securities at any time of the day between 8 and 11:30 a.m., without regard to their debit balance." (A-179)

(3) "No restrictions were placed on the use to be made of securities taken away, on which a debit balance was owed." (A-179)

(4) "Any debit balance would not be due until 3 p.m." (A-179)

In likely recognition of the indefensibility of the District Court's disposition of SCC's summary judgment motion, neither SIPC nor the Trustee relies upon these observations, or relies upon the record before the District Court to support their arguments here. Indeed, in his 12 page "Statement of the Case", the Trustee makes scant reference to the Stipulation of Fact and relies instead upon an improvised and tendentious narrative (Tr. Br. 3-13) of what he believes are SCC's functions and operations. In short, neither the Trustee nor SIPC champions the District Court's reasoning or approach. Nor can they, since the District Court clearly committed error when—as SIPC candidly remarks (SIPC Br. 7)—it did not feel itself "shackled to the naked intent of the parties under SCC's Rule 7" but instead felt free to consider questions of fact not properly before it. It is, after all, hornbook law that:

"[w]hen a contract is so ambiguous as to require resort to other evidence to ascertain its meaning and that evidence is in conflict, the grant of summary judg-

ment is improper . . .'' *Painton & Co.* v. *Bourns, Inc.*, 442 F.2d 216, 233 (2d Cir. 1971).

The confusion below apparently arose because the parties, relying on a stipulation of fact, both moved for summary judgment. Faced with cross-motions, the Courts below must have mistakenly believed that the entire case had been submitted for final determination. But as this Court has on more than one occasion had to remind Courts of first impression:

> ''cross-motions for summary judgment do not warrant the Court in granting summary judgment unless one of the moving parties is entitled to judgment as a matter of law upon facts that are not genuinely disputed.'' *Heyman* v. *Commerce and Indus. Ins. Co.*, 524 F.2d 1317, 1320 (2d Cir. 1975).

Painton & Co. v. *Bourns, Inc.*, 442 F.2d at 232-33; *American Mfr. Mut. Ins. Co.* v. *American Broadcasting-Paramount Theatres, Inc.*, 388 F.2d 272, 279 (2d Cir. 1967); see *Chanofsky* v. *Chase Manhattan Corp.*, Dkt. No. 75-7288 (2d Cir., Mar. 1, 1976); see also, *United States* v. *Bosurgi*, Dkt. Nos. 75-6013, 75-6053 (2d Cir., Jan. 29, 1976); *Home Ins. Co.* v. *Aetna Casualty & Surety Co.*, Dkt. Nos. 75-7357, 75-7359 (2d Cir., Jan. 13, 1976); *Jaroslawicz* v. *Seedman*, Dkt. No. 75-7299 (2d Cir., Dec. 19, 1975); *Judge* v. *City of Buffalo*, 524 F.2d 1321, 1323 (2d Cir. 1975).

The erroneous disposition of SCC's motion for summary judgment and the unauthorized fact adjudication by the Courts below require reversal and either judgment for SCC on its simple legal argument premised on Rule 7 or a remand to give SCC an opportunity to demonstrate its possessory interest in the disputed securities as well as the clear intention that SCC settlement transactions be for cash.

II

Both the Trustee and SIPC Urge Affirmance Upon Factual Arguments Unsupported and Unsupportable On The Summary Judgment Record Made Below.

While both the Trustee and SIPC urge that a trial was held and the record made below is adequate to support the findings of the District Court, it bears noting that the District Court did not rely on that record or any part of the Stipulation of Facts to justify its decision. Rather than support the decision below, the Trustee rehearses the self-same arguments he made in the Bankruptcy Court and the District Court. The Trustee invites this Court—as he did the Courts below—to ignore the issues of law here, overlook the erroneous disposition of SCC's summary judgment motion, deny SCC its day in Court and determine anew that SCC's as yet unpresented evidence cannot sustain the burden of proof and that, whatever Rule 7 may say, what was intended was a credit rather than cash transaction.

But the Trustee's argument is no more supported by the record than was the decision of the Court below. Indeed, the Trustee's argument does not rest on that record but on an "[a]nalysis of [certain of] SCC's operations" which allegedly (Tr. Br. 25) "demonstrates that the settlement procedure . . . is, in fact, an intra-day extension of credit by SCC comparable to [a] day loan." Closer inspection reveals that the Trustee's analysis of the intent and purpose of SCC Rules and procedures is nothing more than unsubstantiated conjecture.

Fatal to the Trustee's assertion is his concession (Tr. Br. 27) that the "key" to his argument is *proof* that SCC intended to extend credit and had as one of its purposes the extension of credit. There is is no such proof in the record. In fact, there is nothing in the record to support this proposition. It is undoubtedly for this reason that the Trustee resorts (Tr. Br. 25) to an out-of-print, near-half

century old treatise titled, "*The Law of Stock Brokers and Stock Exchanges* (1931)". According to the Trustee (Tr. Br. 29), the passage quoted from that book—written by a Charles H. Meyer, identified only (Tr. Br. 30) as an "impartial observer"—"*suggests* that SCC replaces the broker's day loans" (emphasis supplied). Of course, it does no such thing; that passage does no more than *suggest* that the netting process of SCC reduces the size of, and need for, the day loans a broker requires to support his daily position. And, it is well known that clearing loans remain today an essential part of the brokerage business. In any event, the treatise upon which the Trustee relies is not a part of the record, is not admissible evidence, does not constitute testimony and its author, being deceased, is not subject to cross-examination.

As further support for the Trustee's argument on the credit intent and purpose of Rule 7, the Trustee asserts (Tr. Br. 29) that certain parts of some of SCC's other rules (Rules 6, 13 and 14) contain "a number of provisions typical of loan agreements". The Trustee would gloss over the fact that he can point to nothing in the record to support his argument and is unable to point to any reference to the term "loan" in the SCC-Weis contract.

The Trustee summarizes his argument by concluding (Tr. Br. 31):

> "In summary, we have seen that the debit balance settlement system replaces a loan, has all the characteristics of a loan, and looks like a loan to impartial observers."

Feeling the pinch of the record, the Trustee drops all pretense of relying on the decisions below or the few facts stipulated in this case, by arguing (Tr. Br. 33-38) that the SCC cash settlement transaction was converted to one for credit when SCC took Weis' uncertified check. In this, SIPC joins the Trustee, urging (SIPC Br. 5, 6 See, Br. 11-

13) that: "The undisputed circumstances surrounding Weis' demise"—none of which is in the record—show that "SCC made a conscious decision to deliver the securities in question to Weis . . ." on Weis' credit.

Succinctly stated, what SIPC and the Trustee claim is that SCC intended to, and did in fact, knowingly waive its right to insist on cash in the disputed settlement transaction. Waiver is a classic question of fact—one which neither Court below ever addressed. The record is barren of any testimony or other admissible evidence which would support the claimed intent to waive which the Trustee and SIPC would assign to SCC.

In a final attempt to prevent reversal of the Courts below, the Trustee—without benefit of case authority—asserts that Article 8 the UCC bars SCC's reclamation claim.* The Trustee cites no precedent for this proposition, and neither Court below ever considered the question, even though the Trustee urged both courts to do so in his previously submitted memoranda.

The Trustee argues (Tr. 38-45), as he did below, that SCC cannot claim any interest in the securities delivered to Weis because when Weis picked them up, SCC lost all rights which it may have had. The Trustee relies on § 8-301 which vests in the "purchaser" of a security upon its "delivery" all his transferor's rights and on § 8-313 which governs "delivery" to a "purchaser." The Trustee claims (Tr. Br. 40):

> "Under Section 8-313, there are two separate ways in which delivery to a broker can constitute delivery to

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* In what appears some confusion, the Trustee asserts (Tr. Br. 38) that SCC's position on this appeal is based on In re Perpall, 256 Fed. 758 (2d Cir. 1919) and the "old common law 'retention of title' doctrine." On the contrary, SCC's position is based on universally recognized principles of contract law and the fact that the Courts below erroneously disposed of SCC's summary judgment motion by deciding the issues on the merits.

> a customer. First, a security can be delivered in such a way that it is clearly the property of a specific customer . . . Second, a broker, as the agent of the customer, may receive a security in respect of a customer trade and hold it in bulk segregation . . . such a security has been 'delivered' to the customer and the customer is expressly deemed to be the owner of it. *See* UCC Section 8-313(2) Delivery to Weis customers occurred in this second way."

But this is pure *ipse dixit*. There is nothing in the record which demonstrates that the securities here in issue were "clearly the property of a specific customer" and, similarly, nothing that shows the securities were received "in respect of a customer trade" to be held "in bulk segregation."

SIPC likewise relies (SIPC Br. 7-10) on the same provisions of the UCC. But SIPC advances a wholly different interpretation of § 8-313. According to SIPC, when Weis picked up the securities from SCC, those securities were "delivered" to *Weis*—not Weis' customers—and Weis was the "purchaser" under § 8-313, not, as the Trustee contends (Tr. Br. 40) Weis' customers. But this argument—just as that of the Trustee—is without case support and finds no substantiation in the record. The only thing that is clear from the record is SCC's position as a "purchaser", because Rule 7, on its face, so provides. The unresolved issue in this case is whether Rule 7 intends a cash transaction. If Rule 7 cannot provide the basis for a decision in SCC's favor, a remand is clearly necessary now to resolve the many fact questions in this case and to afford SCC the trial which it was denied by the erroneous disposition of its summary judgment motion.

CONCLUSION

For all of the foregoing reasons, this Court should reverse the erroneous judgments of the Courts below and

remand, directing either that judgment be entered in favor of SCC and against Weis and the Trustee or that a trial be held on the disputed issues of contract interpretation in this case.

Respectfully Submitted,

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Of Counsel:

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UNITED STATES COURT OF APPEALS

FOR THE SECOND CIRCUIT

- -x

In the Matter of :

WEIS SECURITIES, INC., :

Debtor. :

Dkt. No. 75-7648

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STOCK CLEARING CORPORATION, :

Plaintiff-Appellant, :

-against- :

WEIS SECURITIES, INC., and EDWARD S. REDINGTON, as Trustee of Weis Securities, Inc., :

Defendants-Appellees. :

AFFIDAVIT OF SERVICE BY MAIL

- -x

STATE OF NEW YORK)
: ss.:
COUNTY OF NEW YORK)

MARK L. DAVIDSON, being duly sworn, deposed and says:

1. I am a member of the bar of this Court and an attorney associated with the firm of Milbank, Tweed, Hadley & McCloy, attorneys for plaintiff-appellant Stock Clearing Corporation.

2. On March 12, 1976, I caused service, by mail, of two (2) copies of the Reply Brief for Appellant to be made upon George A. Davidson, Esq. of Hughes, Hubbard & Reed, attorneys for defendant-appellee Edward S. Redington, as Trustee of Weis Securities, Inc., and Wilfred R. Caron, Esq. Associate General Counsel of the Securities Investor Protection Corporation, "applicant-appellee", by depositing two (2) true copies thereof enclosed in securely fastened and duly post-paid wrappers in a post office box regularly maintained by the United States Government at One Chase Manhattan Plaza, New York,

New York 10005, directed to each of said attorneys at the addresses designated by them for that purpose in the preceding papers in this action, to wit:

George A. Davidson, Esq.
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Washington, D.C. 20006

Dated: March 12, 1976
New York, N.Y. 10005

Mark L. Davidson
Mark L. Davidson

Sworn to before me this
12th day of March, 1976.

Maureen A. McConville
Notary Public

MAUREEN A. McCONVILLE
NOTARY PUBLIC, State of New York
No. 43-4504373
Qualified in Richmond County
Certificate Filed in New York County
Commission Expires March 30, 1977

Dkt. No. 75-7648

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